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FEDERAL COMMUNICATIONS COMMISSION
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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992; Rate Regulation	)	MM Docket No. 92-266
	)	
Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992; Rate Regulation	)	MM Docket No. 93-215

COMMENTS OF COMCAST CABLE COMMUNICATIONS, INC.,
COX COMMUNICATIONS, INC., AND JONES INTERCABLE, INC.

Comcast Cable Communications, Inc., Cox Communications, Inc., and Jones Intercable, Inc., by their attorneys, submit these comments in response to the Commission's *Seventh Further Notice of Proposed Rulemaking* in the above-captioned proceeding.[1/]

In its *Notice*, the Commission tentatively concludes that the 7.5% mark-up that cable operators are currently permitted to recover on increases in programming costs for channels carried prior to May 15, 1994 is no longer necessary in light of the "total incentive structure provided in our revised going forward rules."[2/] The recently adopted revisions to the

1/ Rate Regulation, *Sixth Order on Reconsideration, Fifth Report and Order, Seventh Further Notice of Proposed Rulemaking*, MM Dkt. Nos. 92-266 and 93-215, FCC 94-286 (rel. Nov. 18, 1994) ("*Sixth Order*").

2/ *Id.*, ¶ 133.

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going forward rules, however, provide no new incentives with respect to programming carried prior to May 15, 1994 and they in no way obviate the need -- which the Commission recognized less than a year ago -- for a markup on external cost increases associated with such programming. The proposed rule change accordingly should be rejected.

INTRODUCTION

In its combined *Second Order on Reconsideration, Fourth Report and Order, and Fifth Notice of Proposed Rulemaking,*[3] the Commission adopted "going forward" rules for determining the amount by which operators would be permitted to increase rates if they added channels to their regulated tiers. Those rules generally allowed operators, in such circumstances, to increase their rates by a small fixed amount (which varied depending on the number of channels of programming provided by the system),[4] plus the net increase in programming costs incurred in connection with the added channels, plus a 7.5% mark-up on those increased costs. At the same time, the Commission also determined that any external cost increases associated with *existing* channels that were incurred after May 15, 1994 -- the effective date of the new rules -- should also include a 7.5% mark-up on the actual costs incurred.

3/ *Second Order on Reconsideration, Fourth Report and Order, and Fifth Notice of Proposed Rulemaking*, 8 FCC Rcd 4119 (1994).

4/ For example, cable systems with 36-46 channels received an extra two cents per month; those with more than 46 channels added one cent. *See* 47 C.F.R. § 76.522(e)(2).

The Commission did not purport to have identified the precise markup necessary to provide cable operators with sufficient incentives to invest in new programming and in enhancements to existing programming. But it concluded that, "in order to help assure the continued growth of programming services, we believe that the mark-up we established at the outset of our going-forward methodology should not be established at a minimal level."[5]

Almost as soon as the new going forward rules and forms were released, it became apparent to many cable operators and programmers that the formula for adding new channels to regulated tiers would not provide adequate incentives to add such channels. The Commission agreed and, in its *Sixth Order on Reconsideration,* adopted a new, alternative going forward formula. Like the old formula, the new one allows operators that add channels to increase rates by programming costs associated with the new channels. But instead of an additional percentage markup (plus one or two cents), the new formula allows an additional fixed mark-up of 20 cents per channel. The total amount of any rate increases that result from the addition of channels is limited to $1.20 over the next two years, and $1.40 over the next three years (the "Operator's Cap"), plus an extra 30 cents that can only be used to cover programming costs (the "License Fee Reserve").

The Commission decided that, with respect to channels added pursuant to this new formula, the 7.5% markup on subsequent

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5/ *Id.* at 4242-43 n. 345.

programming cost *increases* should not apply, because "the per channel adjustment of up to 20 cents for additional channels, in addition to the License Fee Reserve, will provide full and fair compensation to operators adding channels to CPSTs."[6/] The Commission also tentatively concluded that it should eliminate the 7.5% mark-up on programming cost increases associated with previously *existing* channels -- *i.e.*, those channels that were already being carried by systems before the going forward rules for adding channels went into effect on May 15, 1994.[7/] According to the Commission, the mark-up "may no longer be necessary given the total incentive structure provided in our revised going forward rules" and "may create an artificial incentive for the operator to continue to offer programming that the operator would not otherwise continue to offer."[8/]

It is this proposal to eliminate the mark-up on programming cost increases for services carried prior to May 15, 1994 that we address -- and oppose -- in these comments. The new going forward formula provides improved incentives for adding *new* program services, but it does not in any way increase incentives to invest in enhancements to *existing* programming. Moreover, eliminating the mark-up will stifle the growth and development of existing programming by removing from cable operators any significant incentives to pay for such improved programming.

6/ *Sixth Order*. ¶ *83*.

7/ The new, alternative formula may be applied retroactively to channels that were added after May 15, 1994.

8/ *Sixth Order*, ¶ 133.

I. THE REVISED GOING FORWARD RULES DO NOT PROVIDE INCENTIVES TO INVEST IN EXISTING PROGRAMMING.

Precisely how the "total incentive structure" of the new going forward rules is supposed to replace the incentives that the 7.5% mark-up supplied with respect to investments in programming carried prior to May 15, 1994 is a mystery. Nothing in the new formula applies in any way to such previously carried programming, and nothing in the Commission's Notice explains the relationship. It may be that the Commission expected that its 20-cent per channel mark-up would cover not only the initial costs of adding new services but also the costs of nurturing the development of *those* services as their costs increased. But there is no indication in the Commission's decision (or in the Technical Appendix that explains the derivation of the 20-cent mark-up) that the mark-up was intended to support increases in the costs of previously carried programming.

Indeed, the only effect that the new rules would appear to have on investment in existing programming is a *negative* one. To the extent that the old rules provided insufficient incentives to invest in *new* programming, they may have skewed investment towards existing programming. It is hard to imagine, however, how restoring incentives to invest in new programming can simultaneously produce new incentives to invest in existing programming, so that an incentive that was formerly deemed necessary -- *i.e.*, the 7.5% markup -- is no longer required and is now "artificial" and excessive.

II. A PASS-THROUGH WITHOUT A MARK-UP ELIMINATES INCENTIVES TO INVEST IN IMPROVEMENTS TO EXISTING PROGRAMMING.

In contrast to the Commission's explanation for its proposed elimination of the 7.5% mark-up on cost increases for existing programming, its reasons for adopting the mark-up in the first place are no mystery at all. Cable operators invest in new channels of programming and in improvements to existing programming for two reasons -- to increase subscribership and to enhance the value of cable service to existing subscribers. Cable penetration -- the percentage of households, where cable is available, that choose to subscribe -- grew rapidly during the 1980's, but it is becoming increasingly difficult to attract new subscribers with enhancements to regulated tiers of programming. Therefore, it is increasingly the case that the principal reason for investing in new and improved programming is to increase the value that existing subscribers place on cable service by more than the increase in programming costs -- and to recover at least some portion of the difference.

This investment incentive disappears, however, if operators are not permitted to increase rates by more than their increased programming costs. If an operator has no prospect of increasing his profits even if existing subscribers are willing to pay more than the increased costs of the programming to receive it, why would it take the risk that the increased value of the programming to subscribers might be *less* than the increased costs?

What the Commission appeared to have recognized when it adopted the 7.5% mark-up last year was that rate regulation requires a careful balancing to ensure not only that rates are reasonable but also that consumers have available the quantity and quality of services that they prefer and would receive in a competitive marketplace. Regulation is an imperfect tool for balancing these twin objectives in a way that replicates the marketplace. But the mark-up that the Commission adopted at least took into account both sides of the balance. The proposal to eliminate that mark-up does not.

CONCLUSION

For the foregoing reasons, the Commission should reject its proposal to eliminate the 7.5% mark-up on increased costs of programming carried on a system prior to May 15, 1994.

Respectfully submitted,

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